G-012/GR-92-22 ORDER ACCEPTING AND ADOPTING STIPULATION AND OFFER OF SETTLEMENT

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Don Storm	Chair
Tom Burton	Commissioner
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In the Matter of the Request of Western Gas Utilities, Inc. to Increase its Rates for Natural Gas Service

ISSUE DATE: October 15, 1992

DOCKET NO. G-012/GR-92-22

ORDER ACCEPTING AND ADOPTING STIPULATION AND OFFER OF SETTLEMENT

PROCEDURAL HISTORY

I. BACKGROUND

A. Initial Commission Action

On January 9, 1992, Western Gas Utilities, Inc. (Western or the Company) filed a petition seeking a general rate increase of $303,782 or 13%, effective March 9, 1992.

On January 24, 1992, Western supplemented its filing with additional information.

On January 27, 1992, the Minnesota Department of Public Service (the Department) filed a letter with the Commission stating that, although much of the filing was technically unsupported, it now contained provisions in compliance with the relevant Minnesota statutes and rules, and may be considered complete. Based on Western's supplementary filing, the Department recommended that the Commission accept Western's filing.

On February 24, 1992, the Commission issued its ORDER ACCEPTING FILING AND SUSPENDING RATES.

On March 6, 1992, the Commission issued its ORDER SETTING INTERIM RATES authorizing Western to collect additional revenues of $256,000 or 10.9 percent on an interim basis and adopting interim rates effective March 9, 1992. The Commission encouraged the parties to explore settlement to minimize the regulatory cost to this small gas utility.

On March 19, 1992, the Commission issued a Notice of Intervention Deadline. The Notice stated that any person wishing to intervene in this matter should petition for intervention on or before April 3, 1992. No person filed such a petition to intervene.

B. Public Hearings

Administrative Law Judge (ALJ) Allan W. Klein conducted public hearings to receive comments and questions from non-intervening ratepayers on April 13 and 14, 1992 in Delano, Cosmos, and Green Isle. Four members of the public appeared and three spoke in Delano. One appeared and spoke in Cosmos and no one appeared at the Green Isle hearing.

In Delano, two citizens objected to the size of the Company's proposed rate increase. The third attender represented the Delano Public Schools and was concerned about whether the rate case would affect the school's transportation contract with Western. The person speaking in Cosmos expressed no concern about the proposed rate increase.

C. A Stipulation and Offer is Filed

On August 12, 1992, Western and the Department, the sole intervenor in this matter, filed a Stipulation and Offer of Settlement. The parties stated their belief that the Stipulation is in the public interest and results in just and reasonable rates. They requested that the Commission issue an Order accepting and adopting the Stipulation.

The Commission met on September 24, 1992 to consider this matter.

FINDINGS AND CONCLUSIONS

II. JURISDICTION

The Commission has general jurisdiction over the Company under Minn. Stat. §§ 216B.01 and .02 (1990). The Commission has specific jurisdiction over rate changes under Minn. Stat. § 216B.16 (1990). The Commission has authority under Minn. Stat. § 216B.16, subd. 1a (1990) to accept the settlement of a rate case on finding that to do so is in the public interest and is supported by substantial evidence.

III. FURTHER ADMINISTRATIVE REVIEW

Under Minn. Rules, part 7830.4100 any petition for rehearing, reconsideration, or other post-decision relief must be filed within 20 days of the date of this Order. Such petitions must be filed with the Executive Secretary of the Commission, must specifically set forth the grounds relied upon and errors claimed, and must be served on all parties. The filing should include an original, 13 copies, and proof of service on all parties.

Parties have ten days from the date of service of the petition to file answers. Answers must be filed with the Executive Secretary of the Commission and must include an original, 13 copies, and proof of service on all parties. Replies are not permitted.

The Commission, in its discretion, may grant oral argument on the petition or decide the petition without oral argument.

Under Minn. Stat. § 216B.27, subd. 3 (1990), no Order of the Commission shall become effective while a petition for rehearing is pending or until either of the following: ten days after the petition for rehearing is denied or ten days after the Commission has announced its final determination on rehearing, unless the Commission otherwise orders.

Any petition for rehearing not granted within 20 days of filing is deemed denied. Minn. Stat. § 216B.27, subd 4 (1990).

IV. WESTERN GAS UTILITIES, INC.

Western is a wholly owned subsidiary of Natrogas, Inc. Western serves natural gas to approximately 3,500 customers in the communities of Watertown, Delano, Montrose, Waverly, Green Isle, Hamburg, Rockford Park, Lake Crawford, Marystown, and Cosmos, Minnesota.

V. STIPULATION AND OFFER OF SETTLEMENT

The Company's initial filing proposed an annual revenue deficiency of $303,782 and sought a 13 percent rate increase to recover that amount. In their Stipulation, the Department and the Company agreed to a 6.9 percent rate increase to recover a revenue deficiency of $168,033.

	Proposed Deficiency	Stipulated Deficiency
Rate Base	$2,691,521	$2,528,880
Rate of Return	11.4%	11.072%
Required Operating Income	306,833	279,998
Operating Income	125,989	166,865
Income Deficiency	$180,844	$113,133
Revenue Conversion Factor	1.6798	1.4853
Revenue Deficiency	$303,782	$168,033

The changes from the Company's original proposal came in the following areas: rate base, income statement, rate of return (cost of capital), test year operating revenue, conservation, and the class cost of service study (CCOSS). Major parts of the stipulation are presented as follows:

A. Rate Base

Western and the Department agreed to reduce test year rate base by $162,641 to $2,528,880. Eight adjustments resulted in that change: 1) prepaid natural gas: an increase of $2,292; 2) plant and accumulated depreciation: an increase of $217; 3) customer deposits: a reduction of $39,352; 4) deferred taxes: a reduction of $18,784; 5) services to Rahr Malting Company: a net increase of $18,693; 6) contributions in aid of construction (CIAC): a reduction of $42,885; and 7) cash working capital: a reduction of $82,822.

B. Income Statement

Western and the Department agreed to increase test year operating income by $40,876 to $279,998. Eight adjustments account for that change: 1) appliance sales and service: a $28,500 increase; 2) depreciation expense: a $1,313 increase; 3) Rahr Agreement: a net increase of $4,729; 4) rate case expenses: a $6,100 decrease; 5) expenses allocated to the Company's parent company Natrogas: a $59,072 decrease; 6) conservation: a $990 decrease; 7) revenue adjustments: a net increase of $82,134; and 8) income taxes: a $9,638 decrease.

C. Revenue Conversion Factor

Western and the Department calculated a revenue conversion factor based on the various marginal tax rates. The stipulated income deficiency was applied to each of the Federal tax rates starting with the lowest bracket resulting in a reduced stipulated conversion factor: 1.4853.

D. Cost of Capital

Western and the Department stipulated to an overall cost of capital (rate of allowed return on investment) of 11.072 percent, down from the 11.4 percent figure in Western's initial filing. The stipulated rate of return on equity (11 percent) was arrived at through a Discounted Cash Flow (DCF) analysis of 11 natural gas companies which derived a dividend yield of 6.7 percent and a growth rate of 4.3 percent.

E. Test Year Revenue

Western and the Department stipulated to test year operating revenue from gas sales that increased Western's proposed operating revenue by $110,593 to $2,448,255. Adjustments accounting for the increase were made to compensate for growth on the Company's system since the end of the test year, for unusual weather during the test year, and to correct for miscalculations in the original filing. The parties also agreed to adjustments in Western's proposed test year sales volumes.

F. Conservation

1. Conservation Plan

The parties stipulated that the Company's supplemental filing to the rate case application and its most recent conservation improvement plan (filed June 1992) meet the filing requirements of Minn. Stat. § 216B.16 (1990).

2. CIP Tracker Account

Western and the Department stipulated that the Company use a tracker account to accumulate over- and underrecovered CIP costs between rate cases. Under the stipulation, the Company would be authorized to impose a carrying charge, based on its allowed overall rate of return multiplied by the tracker account balance, with true-ups occurring during rate cases.

3. Financial Incentive

Western and the Department stipulated that the Company's financial incentive proposal is appropriate and recommended that the Commission approve it in concept. Under the proposed financial incentive proposal, the Company would be allowed to recover 50 percent of the lost margins that are attributable to CIP programs that provide direct energy savings. Lost margins would be determined on a customer-by-customer basis by comparing each customer's annual energy use in the year before the program starts and the year afterwards. The volumetric amount of energy saved for each customer would then be multiplied by one-half the Company's allowed margin in the current rate case and deferred to the tracker account.

4. Test Year CIP Costs

The parties stipulated CIP expenditures in the amount of $9,425, $990 more than the amount Western proposed in its original filing. The stipulated amount exceeds the minimum spending requirement of .5 percent of gross revenue as required by Minn. Stat. § 216B.241, subd. 1 (a) (1990). The parties proposed no capitalization of Western's CIP expenditures at this time.

G. Class Cost of Service Study (CCOSS)

The CCOSS stipulated to by the parties differed from Western's original CCOSS in three respects, the most significant being the transfer of $567,692 from commodity cost to capacity cost. The stipulated CCOSS suggests that firm and interuptible customers would be subsidized by the flexible rate transportation customers. The inaccuracy of that picture results, according to the parties, from the parties' decision to impute revenue from the flexible rate customers at the standard rate instead of at the discounted rate that the Company would actually collect.

H. Rate Design

Western and the Department stipulated that the $168,033 revenue increase would be allocated among customer classes as follows:

Customer Class	Stipulated Test Year Revenue	Stipulated Revenue Increase		Stipulated Revenue
Firm (Sales):				
Residential	$1,605,462	$113,776	7.1%	$1,719,238
Comm. & Indus.	682,873	48,377	7.1%	731,250
Int. (Sales)	137,282	4,018	2.9%	141,300
Flex. Rate (Trans.)	22,638	1,862	8.2%	24,500
Totals	$2,448,255	$168,033	6.9%	$2,616,283

The parties stipulated to rates for the commodity margins per Mcf and the monthly customer charges as follows:

1. Firm (Sales) Gas Service

Commodity Margin/Mcf	$ 1.7591
Residential, Small Commercial & Industrial/month	$ 3.75
Large Commercial & Industrial/month (>250 Mcf/year)	$ 7.50

2. Interruptible (Sales) Gas Service

Commodity Margin/Mcf	$ 1.2353
Customer Charge/month	$ 28.50

3. Flexible Rate (Transportation) Service

Commodity Margin/Mcf	$ 1.2353
Customer Charge/month	$ 28.50

Other stipulated items having implications for the rate design were the Company's extension policies and reconnection fee. The parties proposed a set of detailed tariffs covering extensions, stipulating to a 100 foot extension allowance for service lines and a 220 foot allowance for main extensions for residential customers. Extensions exceeding the footage allowance would be charged $2.75/foot for service lines and $3.35/foot for mains. As to the reconnection fee, the parties stipulated to a fee of $20 during normal working hours, $35 at all other times and a $20 per check non-sufficient funds fee.

VI. COMMISSION ACCEPTANCE AND ADOPTION OF THE STIPULATION AND OFFER OF SETTLEMENT

The Commission finds that the Stipulation and Offer of Settlement is supported by substantial evidence, and represents a just and reasonable resolution of all individual issues raised in the rate case, promotes the public interest, and will result in just and reasonable rates. The Commission will accept and adopt the Stipulation and Offer of Settlement.

A. Substantial Evidence

The Commission bases its rate case decisions on the record. The Commission will approve no rate increase unless it is supported by substantial evidence in the record. In this case, the record is composed of all filings of the parties, the most critical and persuasive of which is the parties' Stipulation and Offer of Settlement (the stipulation). The Commission has examined this document thoroughly and finds that it does not simply recite the agreements made by the parties but provides adequate support for the rate increase that it proposes.

B. Reasonable Resolutions of Individual Issues

In non-ratemaking settlement negotiations it is common for parties to concede some issues to obtain a more favorable resolution of others they value more highly. This is reasonable and appropriate in private disputes, where the goal of the settlement process is to reach a result satisfactory to all parties. In Commission proceedings, however, the goal of the process is to serve the public interest. This requires protecting the interests of the Company, the public, and all customer classes, whether or not their interests are vigorously represented. It requires resolving issues within the bounds of acceptable regulatory practice, since future rate structures are built on the foundations established in past rate cases. For these reasons the Commission scrutinizes settlements with care and requires documentation of the reasonableness of the disposition of issues.

Having examined the record in this case, the Commission finds that the resolutions reached by the parties on the issues are just and reasonable.

Because the Commission is convinced that the stipulation's resolution is in the public interest and is supported by substantial evidence, thorough reasoning, and sound public policy, the Commission will accept and adopt it.

Clarifying comments on some specific issues are as follows:

1. Cost of Capital

The Commission finds that the stipulated overall rate of return is reasonable and leads to just and reasonable rates. The capital structure presented by the parties as part of their support for that rate is unsatisfactory, however, and is not approved as such. The Commission previously approved a capital structure for the Company which contained 46.2 percent equity. Docket No. G-012/S-86-560. In the intervening years, Western issued debt without Commission approval, leaving the Company with an equity ratio of 18.1 percent, which is very low relative to other gas utilities. Only somewhat mitigating this unreasonably low figure is the fact that a major creditor of the Company is its parent corporation Natrogas. Natrogas has lent Western 40.9 percent of its total capitalization. Should difficulties arise over cash flow to pay operating costs and debt service, Western is more likely to successfully negotiate with its parent corporation than with an outside lender. The Commission expects the Company to take steps to improve its equity ratio. The Company is formally reminded of the requirement of Minn. Stat. § 216B.49, subd. 3 (1990) that it must obtain Commission approval before issuing securities. See Ordering Paragraph 7.

2. Conservation

The Commission agrees that the stipulated manner of recovering approved CIP expenditures is appropriate. The parties' plan is consistent with the Commission's decisions to allow other Minnesota utilities to use tracker accounts and carrying charges for their CIP costs between rate cases.

Regarding the financial incentive adopted in this Order, the Commission clarifies that this is concept approval only. Western's current CIP project does not qualify for a financial incentive because it is an energy audit program that does not provide direct energy savings. If the Company ever intends to implement its financial incentive proposal in conjunction with a specific CIP project it would need to get the Commission's advance approval for implementing the incentive. Any future filing should include a specific proposal for how the Company would measure energy savings.

As to Western's test year CIP costs, the Commission notes that none of the Company's CIP expenditures are properly considered capital investments and if the Company would like to capitalize its CIP expenditures in the future it will have to submit a proposal to do so.

3. Base Cost of Gas

The Commission finds that it would be appropriate for Western to zero-out its purchased gas adjustment (PGA) and restate its base cost of gas at the same time it files new tariff sheets in compliance with this Order. The Commission finds it appropriate to include the commodity cost of gas from storage in calculating Western's base gas costs.

4. Technical Corrections to Stipulation

The CCOSS appearing in the Stipulation contains inadvertent errors. The parties indicated that the following is the accurate CCOSS that they intended to present.

Corrected Class-Cost-of-Service-Study

Customer Class	Customer Cost	Capacity Cost	Commodity Cost	Total Cost
Resident'l	$ 417,647	$ 666,648	$ 643,072	$1,727,367
Commer. & Indust.	143,698	299,718	285,542	728,958
Interrupt.	61,798	-0-	83,763	145,561
Transport.	14,397	-0-	-0-	14,397
Totals	$ 637,540	$ 966,366	$1,012,377	$2,616,283

VII. REFUND

In its March 9, 1992 Order in this matter, the Commission authorized Western to charge rates adequate to increase annual revenues by $256,000 beginning March 9, 1992. In that same Order, the Commission directed the Company to keep records of sales and collections under interim rates as would be necessary to compute a potential refund.

In this Order, the Commission has approved a lower revenue increase than it approved in the Interim Rates Order and will therefore, order rates that are also lower than interim rates. Western will be required to refund the excess amount collected under the interim rate schedule, with interest, pursuant to Minn. Stat. § 216B.16, subd. 3 (1990).

To initiate the refund process, the Commission will direct Western to file a proposed plan for refunding with the Commission and other parties in the proceeding within 30 days of the date of this Order. The Department will have 10 days to file comments on Western's proposed refund plan.

ORDER

1. The Commission accepts and adopts the Stipulation and Offer of Settlement as corrected above in part V, B, 4. That document is incorporated by reference into this Order.

2. Within 30 days of the date of this Order, the Company shall file with the Commission for its review and approval, and serve on all parties to this proceeding, revised schedules of rates and charges reflecting the provisions of this Order.

3. Within 30 days of the date of this Order, the Company shall submit its restated base cost of gas, zeroing-out its purchased gas adjustment (PGA) at the effective date of the final rates.

4. Within 30 days of the date of this Order, the Company shall file and serve on all parties to this proceeding proposed customer notices explaining the final rates it proposes to charge.

5. Within 30 days of the date of this Order, the Company shall file and serve on all parties to this proceeding a proposed plan for refunding with interest calculated at the average prime rate the amount by which interim rate revenues exceeded final revenues approved herein.

6. Comments on any Company filing required under this Order shall be filed within 10 days of the Company's service of the filing.

7. Western shall comply with the statute and rules regarding issuance of securities: Minn. Stat. § 216B.49 (1990) and Minn. Rules, parts 7825.1000 - .1500.

8. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Richard R. Lancaster
Executive Secretary

(S E A L)